DOE/IG-0498

# AUDIT REPORT

# BECHTEL JACOBS COMPANY LLC'S MANAGEMENT AND INTEGRATION CONTRACT AT OAK RIDGE

MARCH 2001

U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDIT SERVICES

March 21, 2001

MEMORANDUM FOR THE SECRETARY

FROM: Gregory H. Friedman (Signed)
Inspector General

SUBJECT: INFORMATION: Audit Report on "Bechtel Jacobs Company LLC's Management and Integration Contract at Oak Ridge"

**BACKGROUND**

In December 1997, the Oak Ridge Operations Office entered into a $2.5 billion management and integration contract with Bechtel Jacobs Company LLC (Bechtel Jacobs) for environmental remediation activities at Department of Energy (Department) sites in Oak Ridge, Tennessee; Portsmouth, Ohio; and Puducah, Kentucky. A primary objective was to accelerate cleanup activities and maximize cost effectiveness. To this end, the Department chose a strategy in which the contractor was to rely on competitively-awarded, fixed-price subcontracts for much of the work. The Department, based on its experience, anticipated that the use of competitive, fixed-price subcontracts would result in improved performance and cost savings. In response to the request for proposals, Bechtel Jacobs stated that it would subcontract just over 90 percent of the work to be performed and reduce staffing by about 80 percent, through transitioning staff to subcontracts. This was to be achieved within two years of the contract award. These factors were, in large part, the basis of the award to Bechtel Jacobs.

The objective of this audit was to determine whether Bechtel Jacobs met these commitments.

RESULTS OF AUDIT

Bechtel Jacobs did not use competitive, fixed-price subcontracts or reduce staffing to the extent proposed. In fact, as of September 30, 2000, nearly three years after award of the contract, Bechtel Jacobs had subcontracted less than 60 percent of the original work scope. Further, the contractor had reduced staffing through transition to the subcontractors by only 58 percent. The audit disclosed that the Oak Ridge Operations Office had not incorporated these requirements in the Bechtel Jacobs contract, limiting the Department's ability to hold the contractor accountable for achieving these goals. Bechtel Jacobs, in an attempt to explain the disconnect between its original proposal and actual performance, stated that managing and integrating the work was more difficult than anticipated. We concluded, however, that the Department could have saved an additional $44.1 million in Fiscal Year 2000 had Bechtel Jacobs met the initial terms of its proposal.

MANAGEMENT REACTION

Management disagreed with the audit conclusions but concurred in the recommendations. Management stated that the audit failed to take into account that the Bechtel Jacobs contract was a "first of a kind" award for the Department with significant subcontracting and workforce transitioning provisions. Management also contended that Departmental policy decisions impacted the contractor's ability to meet its subcontracting goals. Also, management believed that the audit should have focused on compliance with the actual contract provisions rather than statements made during the source selection process.

In our audit work, we were cognizant of the fact that the Bechtel Jacobs contract includes unique subcontracting and workforce transition provisions. With regard to the contention that the Department's actions impacted the contractor's ability to meet the subcontracting goals, based on the information available, there was no practical way to confirm that this was the case and, if so, the extent to which it was a factor in the situation. Bechtel Jacobs' made specific commitments regarding subcontracting and staffing during the contractor selection phase of the award process. Because these were significant considerations in the award of the $2.5 billion contract to Bechtel Jacobs, we believe that the contract should have included formal performance expectations reflecting the contractor's commitments.

Attachment

cc: Director of Procurement and Assistance Management

# BECHTEL JACOBS COMPANY LLC'S MANAGEMENT AND INTEGRATION CONTRACT AT OAK RIDGE

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# OVERVIEW

## INTRODUCTION AND OBJECTIVE

Over the past decade, a recurring theme of internal and external reviews has been the Department of Energy's (Department's) need to improve its contracting practices. In response, the Secretary of Energy created a Contract Reform Team (Team) to look at the complete range of the Department's contracting practices. In February 1994, the Team issued *Making Contracting Work Better and Cost Less: Report of the Contract Reform Team*, which identified increased competition as one of the main elements of contract reform.

In order to increase competition, the Department has structured a number of recent solicitations for management contracts (e.g., Rocky Flats Environmental Technology Site, 1995; Hanford Site, 1996; and Savannah River Site, 1996) to foster teaming arrangements. One type of teaming arrangement is the management and integration (M&I) contract. Under this type of contract, a contractor with specialized project integration skills manages the site, overseeing and integrating the work performed by a number of specialized subcontractors.

In December 1997, the Oak Ridge Operations Office (Operations Office) entered into a $2.5 billion M&I contract with Bechtel Jacobs Company LLC (Bechtel Jacobs) to clean up Department sites in Oak Ridge, Tennessee; Portsmouth, Ohio; and Paducah, Kentucky over a 5 ½ year period. One of the primary objectives of the contract was to accelerate cleanup and maximize cost effectiveness through the use of competitive, fixed-price subcontracts. In response to the request for proposals, Bechtel Jacobs stated that it would subcontract 93 percent of the work and reduce staffing by about 82 percent within the first 2 years. The contract was awarded to Bechtel Jacobs, based in part, on these commitments.

The objective of this audit was to determine whether Bechtel Jacobs used competitive, fixed-price subcontracts and reduced staffing as proposed.

## CONCLUSIONS AND OBSERVATIONS

Bechtel Jacobs did not use competitive, fixed-price subcontracts or reduce staffing as proposed. In fact, as of September 30, 2000, Bechtel Jacobs had subcontracted only 58 percent of the original work scope and reduced staffing by only 58 percent. This occurred because the Operations Office did not contractually require Bechtel Jacobs to perform to the proposed levels. In addition, Bechtel Jacobs stated that managing and integrating the work was more difficult than anticipated. The Department could have saved an additional $44.1 million in Fiscal

Year (FY) 2000 had Bechtel Jacobs subcontracted the work and reduced staffing as proposed.

The Office of Inspector General (OIG) is currently performing a separate audit to determine whether the Operations Office held Bechtel Jacobs accountable for achieving performance objectives included in the M&I contract. Bechtel Jacobs received about 98 percent of the available fee in FY 1999. Also, the OIG performed an audit of Bechtel Jacobs' implementation of contractual payroll creation provisions in FY 1999. The OIG concluded in report ER-B-99-06, *Audit of Bechtel Jacobs Payroll Creation* (April 1999), that the Department could not determine if Bechtel Jacobs met its new payroll commitment.

The current audit identified issues that management should consider when preparing its yearend assurance memorandum on internal controls.

Signed
Office of Inspector General

**Bechtel Jacobs Did Not Perform to the Levels Proposed**

Bechtel Jacobs did not use competitive, fixed-price subcontracts or reduce staffing as proposed. As of September 30, 2000, only 58 percent of Bechtel Jacobs' original work scope was subcontracted, and only 58 percent of the employees were transitioned to subcontractors.

Although Bechtel Jacobs proposed to subcontract 93 percent of the work, only 58 percent of the original work scope was actually subcontracted. For the remaining 42 percent of the work scope, Bechtel Jacobs used contracts established by the Department with other contractors at the Oak Ridge Reservation, Portsmouth, and Paducah to perform 24 percent of the work on a cost reimbursement basis. The work performed by the other Department contractors included a wide variety of areas such as environmental monitoring, technical support, and dosimetry services. Bechtel Jacobs performed the remaining 18 percent of the work. Originally, Bechtel Jacobs planned to perform 7 percent of the work including general program support, project support, and project execution activities. However, after the contract was awarded, Bechtel Jacobs began to perform work in several other areas including East Tennessee Technology Park fire, security, and emergency duties.

Further, Bechtel Jacobs only transitioned 58 percent of the workforce to subcontractors despite its proposal to keep the staffing level to fewer than 400 employees, which would have been an 82 percent reduction. As of September 30, 2000, Bechtel Jacobs' staffing level had decreased to 910, which is 510 more employees than Bechtel Jacobs originally proposed. About 144 of the 510 employees were performing work Bechtel Jacobs originally planned to subcontract. Also, new work scope performed at the Operations Office's direction accounted for another 134 employees. The remaining 232 employees were performing core functions such as procurement and project management.

**A Primary Objective Was to Accelerate Cleanup and Maximize Cost Effectiveness**

According to the request for proposals, one of the primary objectives of the M&I contract was to accelerate cleanup and maximize cost effectiveness through the use of competitive, fixed-price subcontracts. In response to the request for proposals, Bechtel Jacobs stated that it would subcontract 93 percent of the work scope and reduce staffing by about 82 percent within the first 2 years. The Source Evaluation Board (SEB) evaluated all proposals received in response to the request for proposals, and determined that Bechtel Jacobs' proposal was the most advantageous to the Government.

The proposals were evaluated to determine the extent they demonstrated a thorough understanding of, and capability to successfully accomplish, the statement of work focusing on the Oak Ridge 2006 Plan. Strengths and weaknesses of the proposals were evaluated based on the following five factors and the weights assigned to each in the evaluation process:

| Factors | Percentage Weight |
|---|---|
| Technical Approach | 30 |
| Management and Organization | 30 |
| Community Investment | 20 |
| Transition Plan | 15 |
| Corporate Experience and Past Performance | 5 |

The SEB considered Bechtel Jacobs' commitment to subcontract 93 percent of the work to be a strength of its technical approach. The SEB also considered Bechtel Jacobs' commitment to reduce staffing by about 82 percent to be a management and organizational strength.

**Performance at the Proposed Levels was Not Contractually Required, and Bechtel Jacobs Stated Managing and Integrating the Work was Difficult**

Bechtel Jacobs did not perform at the levels it originally proposed because (1) the Operations Office did not contractually require Bechtel Jacobs to perform at the proposed levels, and (2) Bechtel Jacobs stated managing and integrating the work was more difficult than anticipated.

The Operations Office did not develop contractual requirements or incentives to ensure Bechtel Jacobs worked to the proposed levels. Although the Operations Office established performance measures in accordance with the Government Performance and Results Act of 1993, attaining these performance measures would not ensure that the objectives of the contract would be met. Subcontracting and workforce transitioning were two of the primary objectives of the contract; however, specific amounts for each factor were not included as contractual requirements or performance-based incentives when the contract was awarded. As a result, there was little incentive for Bechtel Jacobs to maximize cost effectiveness through the use of competitive, fixed-price subcontracts or staff reductions.

The Operations Office did establish performance-based incentives for Bechtel Jacobs in FYs 1999 and 2000. In FY 1999, Bechtel Jacobs earned incentive fees totaling $1 million for completing the FY 1999 subcontracting actions listed in its Integrated Subcontracting Strategy, and earned another $1 million for reducing its core staffing by 46 percent. In FY 2000, Bechtel Jacobs earned incentive fees totaling $500,000 for awarding critical FY 2000 subcontracts. However, no performance incentives related to staff reductions were established in FY 2000.

In addition, Bechtel Jacobs stated that it did not subcontract the work to be performed or reduce staffing as proposed because managing and integrating the work was more difficult than originally anticipated. For example, Bechtel Jacobs stated that it was not practical to subcontract some types of work, such as emergency services, because complex jurisdiction and coordination issues existed. Also, Bechtel Jacobs stated that it needed more legal and procurement personnel than originally anticipated due to the sheer number of subcontractors involved in performing the scope of work.

**Department Could Have Saved $44.1 Million in FY 2000**

We estimated the Department could have saved an additional $44.1 million in FY 2000 had Bechtel Jacobs subcontracted the work and reduced staffing to the levels proposed. Bechtel Jacobs estimated that for the subcontracts awarded, it expected to save 29.7 percent over revised baseline amounts. By applying the 29.7 percent rate to the work currently being performed by other Department contractors and in-house, we estimated that the Department could have saved an additional $19.2 million in FY 2000 had Bechtel Jacobs subcontracted 93 percent of its original work scope. Bechtel Jacobs also proposed that 7 percent of its contract costs would be spent performing core M&I functions. However, Bechtel Jacobs spent $52.7 million (13 percent) in FY 2000 on core M&I functions, a difference of $24.9 million.

## RECOMMENDATIONS

We recommend that the Manager, Oak Ridge Operations Office:

1. Ensure future M&I contracts require, or provide incentives for, performance at the levels proposed during source selection and consistent with the Department's procurement objectives;

2. Direct Bechtel Jacobs to analyze work performed by other Department contractors and subcontract additional areas that could be performed on a competitive, fixed-price basis; and,

3. Direct Bechtel Jacobs to analyze core staffing levels and reduce staffing in areas where additional workforce transitioning could be employed.

## MANAGEMENT REACTION

Management concurred with the recommendations, but disagreed with the audit conclusions. Management stated that the OIG failed to take into account that the Bechtel Jacobs contract was a "first of a kind" award for the Department with significant and unique subcontracting and workforce transition provisions, and that the Department's policy decisions impacted the contractor's ability to meet its subcontracting goals. Also, management believed that the assumption that 29.7 percent cost savings would be achieved with additional subcontracting was an inaccurate extrapolation of savings from earlier awards. Finally, management believed the OIG should have focused on compliance with the actual contract provisions rather than statements made during the source selection process. Management's specific comments, organized by recommendation, are as follows:

<u>Recommendation 1</u>: Management stated that it intended to include definitive requirements, as appropriate, on a case-by-case basis in future contracts. Management also stated that it specifically decided not to include definitive requirements for subcontracting plans, workforce transitions plans, or staffing plans in the Bechtel Jacobs contract based on lessons learned from earlier procurements. That decision was largely due to anticipated, but undefined, specific changes that would occur during the transition period. Management reported that as a result of its experience with the Bechtel Jacobs M&I contract, it was now in a better position to identify specific requirements, which may be appropriate for incorporating into future contracts.

<u>Recommendation 2</u>: Management stated it would direct Bechtel Jacobs to complete a review of planned FY 2002 work to identify any additional opportunities for subcontracting. The review will address both Bechtel Jacobs work planned for self performance and planned work authorization to UT-Bechtel, LLC and BWXT-Y12, LLC and will be completed by July 2001. The results of this review will be incorporated into the FY 2002 update to the Life-Cycle Baseline prior to the beginning of the fiscal year, consistent with approved funding, work prioritization, and sequencing.

<u>Recommendation 3</u>: Management stated that it will conduct a review of Bechtel Jacobs' staffing levels to determine if there are

opportunities for additional workforce transition or staffing reductions. The review is planned to be completed by the end of May 2001.

**AUDITOR COMMENTS**

Management's planned actions are considered to be responsive. We acknowledge that Bechtel Jacobs' contract includes unique subcontracting and workforce transition provisions; however, we could not determine whether the Department's actions impacted the contractor's ability to meet its subcontracting goals. Still, we believe the Department should have required Bechtel Jacobs to perform to its proposed levels, or to lower levels if warranted by changes in Departmental policy or other factors. Also, we estimated the potential cost savings based on the rate of cost savings reported by Bechtel Jacobs for previous fixed-price subcontracts (29.7 percent) applied to 93 percent or the original scope of work. Since the Department awarded a $2.5 billion contract on the basis of Bechtel Jacobs' proposal, our audit focused on the requirements that, in our opinion, should have been included in the contract.

# Appendix

**SCOPE**

The audit was performed from September 14, 2000, to January 8, 2001, at the Oak Ridge Operations Office and the East Tennessee Technology Park. The scope of the audit included the Operations Office's procurement activities as well as Bechtel Jacobs' subcontracting and workforce transitioning activities from April 1998 through September 2000.

**METHODOLOGY**

To accomplish the audit objective, we:

- Identified the Operations Offices' objectives for the M&I contract;
- Reviewed Federal and Department regulations governing contract solicitation;
- Examined Operations Office procurement files;
- Evaluated the status of the workforce transition;
- Analyzed the costs associated with M&I contract activities;
- Calculated the amount of work Bechtel Jacobs performed in-house, subcontracted out, and assigned to other Department contractors;
- Discussed subcontracting and workforce transitioning activities with Department and contractor personnel; and,
- Reviewed the Operations Office's compliance with the Government Performance and Results Act of 1993.

The audit was performed in accordance with generally accepted Government auditing standards for performance audits and included tests of internal controls and compliance with laws and regulations to the extent necessary to satisfy the audit objective. Accordingly, the audit included reviews of Operations Office procurement activities as well as Bechtel Jacobs subcontracting and workforce transitioning activities. Because our audit was limited, it would not necessarily have disclosed all internal control deficiencies that may have existed at the time of our audit. We conducted a limited reliability assessment of computer-processed data and found that the associated internal controls were adequate.

We held an exit conference with the Acting Chief Financial Officer, Oak Ridge Operations Office, on March 5, 2001.

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